

LEGAL UPDATES

PUBLISHED: SEPTEMBER 5, 2023

Service

Private Wealth

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Special Needs Planning: Special Needs Trusts and ABLE Accounts

Estate planning can be a daunting task for individuals and families. The stakes can be high. The decisions are often numerous. Family dynamics frequently come into play. However, for those living with special needs or those who have loved ones with special needs, estate planning raises additional issues:

What if my child won't ever be able to manage their own finances?

How can I set aside money for my special needs adult child without affecting their eligibility for government benefits?

What if I receive a large cash bequest that jeopardizes my Supplemental Security Income?

What if I am the beneficiary of a trust that disqualifies me for Medicaid?

These are the kinds of questions and concerns that arise when attempting to plan for persons with special needs. Fortunately, individuals and families have tools at their disposal that address these problems and provide a safer financial future for the special needs individual. Two of the most common tools are Special Needs Trusts (SNTs) and ABLE Accounts.

Special needs trusts

An SNT is a trust specifically designed to hold assets for an individual receiving government benefits without jeopardizing the individual's eligibility for those benefits. This is important because many government benefits, such as Supplemental Security Income (SSI) and Medicaid, are "means-tested," meaning that an individual's eligibility for the benefits depends on his or her income and assets. For example, the 2023 countable resource limit for individuals to receive SSI is \$2,000. A simple outright cash gift of \$10,000 would put an individual far over that limit and disqualify them from receiving

SSI along with other government benefits. The same goes for gifts made through traditional revocable and irrevocable trusts.

Enter the SNT. SNTs provide many of the benefits associated with ordinary irrevocable trusts like creditor protection and a trustee who manages assets on behalf of the beneficiary. However, unlike traditional trusts, SNTs do not count towards a beneficiary's countable assets for the purposes of government benefits eligibility. SNTs accomplish this by placing certain restrictions on the use of assets contained in the SNT. These restrictions are why assets within SNTs are not considered countable assets – because the beneficiary has much less access to the assets in a SNT, the government does not consider those assets “countable” for the purposes of determining eligibility for benefits.

The restrictions mainly relate to when and how SNT assets can be used. A primary restriction is on rights of withdrawal. In a typical irrevocable trust, a beneficiary usually has the right to withdraw a certain amount of assets from the trust at a given interval. The beneficiary of a SNT, on the other hand, has no right to withdraw or demand funds or distributions from the SNT. The trustee ultimately decides when to use the SNT assets. Another important restriction is on the types of expenses for which SNTs can pay. The trustee of an SNT may only use assets for the beneficiary's supplemental needs, such as medical expenses, supplemental or support services not covered by benefits, rehabilitation services, education, recreation, and clothing, but not for ongoing support such as rent, basic utilities, groceries, or cash payments to the beneficiary. SNTs are therefore less like a transfer of wealth to a special needs beneficiary and more like a reserve of assets ready to supplement a special needs individual's government benefits. For these reasons, SNTs are often referred to as “Supplemental Needs Trusts.”

Two types of SNTs: Third Party SNTs and First Party SNTs

There are two types of SNTs: Third Party SNTs and First Party SNTs. Third Party SNTs are the variety most people think of when considering an SNT. To create a Third Party SNT, a third party (hence the name Third Party SNT), typically a parent or a relative, places some of their own assets into an SNT for the benefit of a special needs individual. The third party may form a Third Party SNT as a standalone irrevocable or revocable trust, as a subtrust under a revocable trust structure, or as a testamentary trust through a last will and testament. There is no limit on the amount of assets that a Third Party SNT may hold, and upon the death of the beneficiary there is no requirement that the trust assets be used to reimburse the government for benefits paid during the beneficiary's lifetime, as with a First Party SNT (discussed below). The entirety of the remaining trust assets can be distributed to remainder beneficiaries named in the trust.

A First Party SNT is an irrevocable trust where the special needs individual uses their own assets to establish a SNT. These most commonly arise when an individual with existing assets becomes

disabled due to an event like an injury – if they wish to qualify for government benefits, they may reduce their countable assets by putting the assets into a First Party SNT (subject to a “look-back” period, discussed below). Critically, third parties should never contribute assets to a First Party SNT. Unlike a Third Party SNT, a First Party SNT must contain provisions to reimburse the government after the beneficiary’s death for any benefits paid on their behalf during their lifetime. The government imposes this requirement as a tradeoff – in exchange for allowing the special needs individual to retain their assets in a SNT, the trust must pay the government back with those assets once they are no longer needed for the beneficiary. After the government program(s) are reimbursed, the remaining trust assets may be distributed to the remainder beneficiaries named in the trust. Lastly, First Party SNTs must be formed before the beneficiary turns 65.

Third Party SNT planning scenarios

As stated above, the typical SNT scenario is one in which a family member or friend sets up the SNT as a standalone trust for the benefit of the special needs individual. If they opt to make the SNT irrevocable, the SNT will have many of the benefits enjoyed by typical irrevocable trusts, such as creditor protection. However, because the trust is irrevocable, funds may not be removed from the SNT, and it is more difficult to amend the terms of the SNT. On the other hand, they can opt to set it up as a revocable SNT. The benefit of a revocable SNT is that if they overfund the SNT or the beneficiary’s government benefits meet all the beneficiary’s needs, the creator of the SNT can pull assets out of the revocable SNT.

Another common scenario involves creating an SNT as a subtrust within a revocable trust. This typically involves a parent with an existing revocable trust. Such a revocable trust will include provisions creating separate irrevocable trusts for each child upon the death of the surviving spouse. If the parents have a special needs child, they can amend the trust with provisions stating that such child’s separate trust shall be a Third Party SNT. The benefit of this revocable trust structure is that the assets in the revocable trust remain the parents’ assets until the surviving spouse’s death.

The last common Third Party SNT scenario involves a testamentary SNT created by a last will and testament. In this scenario, someone leaves the special needs individual a gift in their will. The terms of the will dictate that such gift will be held in an SNT for the benefit of the special needs individual. The will sets forth the terms of the SNT.

A less common Third Party SNT scenario involves an existing irrevocable trust with a special needs beneficiary. For example, assume that a parent creates a revocable trust that breaks into separate irrevocable trusts for each of their children upon the parent’s death. One of the children subsequently becomes disabled through a severe injury, and the parent dies before amending the revocable trust to include SNT provisions for that child. The child is now the beneficiary of a regular irrevocable trust. As stated above, distributions of such assets to that child will most likely be considered countable

assets which could disqualify them from receiving government benefits. To fix this problem, the child needs to convert the regular irrevocable trust into a Third Party SNT. Unfortunately, there is not an easy way to accomplish this. In many states, this will require the child (or his or her conservator) to petition a court to modify the trust through a judicial process. This may be both costly and time consuming. This scenario could have been avoided if the parent had amended their revocable trust prior to their death. The moral of the story here is that it is much easier to plan ahead for an SNT rather than to expect others to try to create one after the fact.

First Party SNT planning scenarios

First Party SNTs typically arise from different scenarios. The most common of these is mentioned above: a formerly abled person with their own assets becomes disabled and must figure out how to become eligible for government benefits. In such a situation, the person can create and place their assets in a First Party SNT. This reduces their countable assets while simultaneously protecting those assets from creditors (subject to a “look-back” period, discussed below).

A less common First Party SNT scenario arises when a special needs individual is due to receive a bequest from a will or an outright distribution from a trust. In this scenario, it is critical to have the executor or trustee hold off on transferring the bequest or gift until the special needs individual (or his or her conservator, if applicable) sets up a First Party SNT. The executor or trustee will then distribute the assets directly into the First Party SNT. If the special needs individual is under a conservatorship, the conservator must inform the court of the pending bequest or distribution and secure the court’s permission to establish the SNT for the benefit of the special needs individual.

If the bequest or distribution is transferred to the special needs individual before an SNT is established, he or she may become ineligible for government benefits. The solution is straightforward, in theory – the special needs individual needs to create a First Party SNT and transfer the bequest or gift to the SNT. The issue in this scenario is that certain programs, like Medicaid, impose a “look-back” period on Medicaid applicants and/or recipients. During the “look-back” period, Medicaid will look back at all the financial transactions made by the special needs individual for the past five years (2.5 years in California). If a special needs individual had assets over the countable assets limit in the past five years, or if he or she has transferred assets out of his or her estate in an attempt to qualify for benefits, Medicaid will implement a penalty, which is typically ineligibility for benefits for a set period of time. Each state has a formula for determining the penalty. Again, as with the Third Party SNT scenario outlined above, it is much easier to create an SNT before the special needs individual receives the assets rather than trying to fix the situation after the fact.

ABLE Accounts

SNTs aren't the only option for special needs individuals. Following the passage of the Stephen Beck Jr. Achieving a Better Life Experience Act of 2014 (the "ABLE Act"), special needs individuals and families of special needs individuals may establish ABLE Accounts. An ABLE Account is a bank account that operates like a 529 Plan. The ABLE Account is either opened by the special needs individual or on the individual's behalf, and the individual, their family, their friends, or their Special Needs Trust may make contributions to the account with after-tax dollars. These assets in the ABLE Account accumulate income tax free and are used for the individual's needs. However, unlike 529 Plans which are intended for education and related expenses, ABLE Account funds may be used for a variety of expenses: education, housing, transportation, legal fees, health, and basic living expenses, to name a few.

ABLE Accounts do impose a number of requirements on the special needs individual. To qualify for an ABLE Account, the special needs individual must be:

receiving Supplemental Security Income (SSI) based on blindness or disability that began before age 26; or

in SSI suspense due solely to excess income or resources but otherwise eligible for SSI based on blindness or disability that began before age 26; or

receiving disability insurance benefits (DIB), childhood disability benefits (CDB), or widow(er)'s disability benefits (DWB) based on blindness or disability that began before age 26; or

the subject of a disability certification.

Additionally, there are limits on how much may be contributed to the ABLE Account in a given year and on the total value of assets in the ABLE Account. An ABLE Account owner, if they work and do not participate in an employer sponsored retirement plan, may contribute up to \$13,590 per year to the ABLE Account. Friends, family, an SNT, or a 529 Plan rollover may each contribute up to \$17,000 annually. A special needs individual may have up to \$100,000 in the ABLE Account and still qualify for SSI. ABLE Plan limits for other programs such as Social Security and Disability Insurance (SSDI) or Housing Assistance from the Department of Housing and Urban Development programs (HUD) range from \$235,000 to \$550,000.

Compared to SNTs, ABLE Accounts provide a relatively simple solution to some of the more basic issues surrounding estate planning for special needs individuals. ABLE Accounts provide a source of funds for various expenses without jeopardizing eligibility for government benefits, and they provide a convenient way of transferring assets to the special needs individual. They do not have the benefit of a trustee overseeing the assets and using their judgment to determine when distributions should be

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made, nor do they accommodate situations where a special needs individual would require assets in excess of the ABLE account limits. In those situations, an SNT is more appropriate.

What this means to you

SNTs and ABLE Accounts are just two tools in the estate planning toolbelt of individuals and families trying to plan around special needs. However, SNTs and ABLE Accounts may be some of the most powerful tools when used correctly and in appropriate situations.

Contact us

If you think that an SNT or an ABLE Account would be a helpful tool for you and your family, contact a member of the Husch Blackwell Private Wealth team or your Husch Blackwell attorney today and schedule a meeting to discuss. Planning today means less headaches tomorrow for both you and your loved ones.